IN THE

Supreme Court of the United States

OCTOBER TERM, 1955

No. 924

HUDSON & MANHATTAN RAILROAD COMPANY,
DEBTOR,

Petitioner,

v.

HERMAN T. STICHMAN, TRUSTEE OF THE DEBTOR,

WILLIAM J. HARDING, JR., IRVING I. SCHNUR AND SHIRLEY REITER, PETITIONING CREDITORS,

AND

SECURITIES AND EXCHANGE COMMISSION

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR HERMAN T. STICHMAN, TRUSTEE OF THE DEBTOR, IN OPPOSITION

Opinions Below

The opinion of the Court of Appeals (Appendix A of the petition), reported in 229 F. 2d 616, affirms two interlocutory orders of the United States District Court for the Southern District of New York, Order No. 28 and Order No. 36. The District Court did not enter an opinion with

respect to Order No. 28; its oral ruling appears at Tr. App. 28.[1] The opinion of the District Court with respect to Order No. 36 was entered orally on March 7, 1955 (Tr. App. 265-6), and has not been reported.

Questions Presented

1. Whether the District Court abused its discretion in refusing to direct a Chapter X trustee to pay the charges of engineers to be employed by a debtor for the purpose of valuing the debtor's property as of the time of the filing of an involuntary Chapter X petition which had already been approved on the basis of the debtor's answer and consent to reorganization.

2. Whether the District Court abused its discretion in refusing to permit a debtor to file an answer *de novo* withdrawing its consent to and prayer for reorganization under Chapter X, months after the District Court, acting upon the debtor's original answer and consent, had approved an involuntary petition.

Statutes Involved

The pertinent provisions of the Bankruptcy Act are set forth in Appendix C of the petition and in Appendix A hereof.

Statement

Petitioner seeks review by this Court of a judgment of the United States Court of Appeals for the Second

[1] The appendix to the Trustee's brief in the Court of Appeals is referred to herein as "Tr. App.", the appendix to the Debtor-petitioner's brief below as "D. App.", and the unprinted record on appeal as "R."

Circuit which affirmed two interlocutory orders of the United States District Court for the Southern District of New York entered during the course of Chapter X proceedings for the reorganization of Hudson & Manhattan Railroad Company, Debtor. Both orders related to petitions filed by the Debtor months after the District Court had approved an involuntary petition under Chapter X on the basis of the Debtor's answer and consent to reorganization.

Order No. 28, entered February 23, 1955 (D. App. 3), denied the Debtor's petition (D. App. 27-35) for an order authorizing it to employ a firm of engineers, at the expense of the estate, to value the Debtor's property as of the date of the filing of the involuntary petition which instituted the proceeding.

Order No. 36, entered April 7, 1955 (D. App. 4-8), denied the Debtor's petition (D. App. 37-44) to withdraw its "amended answer" to the involuntary petition and to file an answer *de novo* withdrawing the consent to and prayer for reorganization under Chapter X contained in both the Debtor's original answer (D. App. 18-19) and its "amended answer" (D. App. 23-4).

On August 11, 1954, three bondholders of the Debtor filed an involuntary petition for a Chapter X reorganization (D. App. 9-16; Tr. App. 280-90). The Debtor moved on extensive affidavits to dismiss on the ground that Chapter X did not apply, asserting that the Debtor was part of the Pennsylvania Railroad's general railroad system and thus was a "railroad corporation" whose reorganization would be governed by Section 77 of the Bankruptcy Act and not Chapter X (R. 730A-CC).

On November 19, 1954, while its motion to dismiss was awaiting decision, the Debtor filed a voluntary petition in a separate proceeding, alleging that it was unable to

meet its debts as they matured and seeking reorganization under Section 77 (D. Ex. 2; R. 723E-H; Tr. App. 161-4).

On November 24, 1954, the District Court appointed a receiver for the Debtor, on motion of the petitioning creditors (R. 723K, 724-8). The Debtor immediately appealed from this order (R. 729).

On December 1, 1954, the District Court entered its opinion and orders denying the Debtor's motion to dismiss the Chapter X proceeding and dismissing the Debtor's petition for a Section 77 reorganization upon the finding that the Debtor was an interurban electric railway not operated as part of a general railroad system, and thus was subject to reorganization under Chapter X and not under Section 77. *In re Hudson & Manhattan R. Co.*, 126 F. Supp. 359. No appeal was taken either from the dismissal of the Debtor's Section 77 petition, or from the denial of its motion to dismiss the Chapter X petition.

The Debtor's decision not to appeal the December 1 orders of the District Court was based on a thorough canvass of the situation by its board of directors on the following day. Upon recommendation of the president of the Debtor, and over the opposition of counsel, the board adopted a resolution instructing counsel to withdraw the appeal from the order appointing a receiver and to file such papers as might be necessary to permit the reorganization of the Debtor under Chapter X (Tr. App. 83-6, 165-9, 238-9, 291-4). The resolution was followed by a public announcement which stated that the action of the board made unnecessary any further litigation regarding the applicable section of the Bankruptcy Act, and that it was expected to lead to the appointment of a trustee within the next few days (Tr. App. 295).

The Debtor's counsel advised the directors on December 6, 1954 that, to protect the directors from personal liability

under the New York Stock Corporation Law, the acts of bankruptcy alleged in the petition should be denied (D. App. 109-10). Counsel were instructed the same day to file a formal answer denying the acts of bankruptcy but joining in the prayer of the petition for reorganization (D. App. 112).

On December 8, 1954, the Debtor's answer and consent to reorganization was served and filed in the Chapter X proceeding. In this pleading, the Debtor, without conceding the applicability of Chapter X, admitted that it was unable to meet its debts as they matured, denied the alleged acts of bankruptcy, consented to its reorganization, and joined in so much of the petition as prayed for reorganization (D. App. 19).

On December 14, 1954, the District Court entered Order No. 10 approving the creditors' petition "due to and by reason of the Debtor's answer and consent to reorganization", and appointing Herman T. Stichman as Trustee of the Debtor (R. 748-57). The Debtor did not appeal from this order (D. App. 6).

On December 22, 1954, an individual stockholder filed an answer to the creditors' petition, denying that the Debtor was insolvent or unable to pay its debts as they mature, but admitting, by failure to deny, the allegations of the petition establishing the Court's jurisdiction under Chapter X (D. App. 21-2).[2]

On December 29, 1954, the Debtor, without applying for leave of the District Court, filed what purported to be an "amended answer and consent to reorganization", served

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[2] Hearings were held on the issues raised by the stockholder's answer. On December 21, 1955, upon the conclusion of these hearings, the original approval of the creditors' petition by Order No. 10 was reaffirmed by the District Court. *In re Hudson & Manhattan R. Co.*, 138 F. Supp. 195. No appeal was taken from the order entered on this opinion, and the time to appeal has expired.

the previous day, which denied that the Debtor was insolvent and certain other allegations of the creditors' petition, in addition to denying (as in its original answer) the alleged acts of bankruptcy (D. App. 23-4). Again the Debtor specifically admitted its inability to meet its debts as they mature, consented to its reorganization, and joined in so much of the creditors' petition as prayed for reorganization.

On February 18, 1955, pursuant to a decision of the Debtor's board of directors that month to join forces with the answering stockholder (Tr. App. 198-200), the Debtor petitioned the District Court for an order authorizing it to employ engineers, at the expense of the estate, to value the Debtor's property as of August 11, 1954 and the four months prior thereto (D. App. 27-35). The petition estimated that the study would require about four months, and sought approval of the charges of the engineers up to $40,000 without further order of the Court.

Thus, for the first time since the determination of the board on December 2, 1954 to proceed promptly with reorganization under Chapter X, the Debtor asserted that the District Court's determination of insolvency was a condition precedent to the reorganization of the Debtor (D. App. 29). The District Court ruled that the Debtor's answer had eliminated insolvency as an issue material to the Court's jurisdiction, and that the Debtor was barred from contesting the issue (Tr. App. 24, 28). It entered Order No. 28, denying the Debtor's petition.

The Debtor then sought to reverse completely the position taken in its answer and consent to reorganization. On March 1, 1955, the Debtor moved for leave to withdraw its "amended answer and consent to reorganization" and for leave to answer *de novo* (D. App. 36-7). The proposed answer *de novo* would have omitted the Debtor's consent to reorganization under Chapter X, its joinder in the prayer

for reorganization, and its specific admission that it was unable to meet its debts as they mature, but would have continued to admit its inability to pay debts by failure to deny that allegation of the creditors' petition (D. App. 43-4).

Following a full hearing of the Debtor's evidence and argument, the District Court announced its decision denying the Debtor's petition upon findings that it lacked merit and that it was not filed in good faith (Tr. App. 1-266). Following another hearing on the form of order (Tr. App. 267-79), the District Court entered Order No. 36, denying the petition on those grounds.

Argument

1. The judgment of the Court of Appeals, affirming two interlocutory orders of the District Court, does not present the questions stated in the petition. Both are orders which could properly be entered by the District Court, as a matter of discretion on the facts before the Court, however the questions stated in the petition might be determined.

Order No. 28 denied a petition of the Debtor to charge the estate with engineers' fees up to $40,000, before any services had been rendered. Even if the issue of insolvency had been material at the stage of the proceeding when the Debtor's petition was made, there nevertheless was no statutory basis for directing the Trustee to pay the charges of engineers to be employed either by creditors to prove insolvency or by the Debtor to prove solvency. The Bankruptcy Act does not contemplate that litigants will have their fees and expenses financed in advance by the estate. Compensation for services and reimbursement of expenses is allowed only after services have been rendered and their

value to the estate is known. Bankruptcy Act, §§241-243, 11 U. S. C. §§641-643.

Order No. 36 denied the Debtor's petition, addressed to the discretion of the District Court, for leave to withdraw an answer months after it had been filed and the issues adjudicated, on the ground that it was not filed in good faith as well as its lack of merit. On the record, as held by the Court of Appeals, there is ample support for the finding of lack of good faith.

The denial of neither petition thus presents any question of law appropriate for review by this Court.

2. The jurisdiction of the District Court to proceed with the reorganization of this Debtor under Chapter X of the Bankruptcy Act was determined by the District Court on December 1, 1954, not only by an order in this Chapter X proceeding, but also by an order in the separate proceeding instituted by the Debtor under Section 77. That determination of jurisdiction is *res judicata* of the issue, and is not subject to collateral attack. *Stoll* v. *Gottlieb*, 305 U. S. 165 (1938); *Baldwin* v. *Iowa State Traveling Men's Association*, 283 U. S. 522 (1931).

The District Court's Order No. 10 of December 14, 1954, approving the creditors' petition and appointing a Trustee upon the basis of the Debtor's answer and consent to reorganization, had become final before the filing of either of the Debtor's petitions denied below, and has never been appealed. Under Section 149 of the Bankruptcy Act, as well as under the cases cited above, that order constitutes a conclusive determination of the jurisdiction of the Court in so far as the Debtor is concerned. Such an order is subject to review by appeal, but not by collateral attack after the time to appeal has expired.

Moreover, as held below, the District Court determination of the Chapter X-Section 77 jurisdictional issue was well supported by the facts and the law (petition, p. 35).

3. Under Chapter X, a debtor can make unnecessary the proof of an act of bankruptcy otherwise required by Section 131 in involuntary proceedings by filing an answer which embodies the substance of a voluntary petition. Indeed, such an answer is itself an act of bankruptcy under Section 3a(6) of the Bankruptcy Act, 11 U. S. C. §21a(6). Since a debtor which desires reorganization cannot file a voluntary petition when an involuntary petition is pending (Section 126, 11 U. S. C. §526), this form of answer enables such a debtor to obtain prompt relief under Chapter X. Compare *Moore* v. *Linahan*, 117 F. 2d 140, 143 (2d Cir. 1941), cert. denied 314 U. S. 628 (1948).

4. Whether the Debtor was entitled, without leave of the Court, to amend its answer 20 days after the answer was filed and 14 days after the District Court's final determination of the issues to which the answer was directed, is not relevant to the petition herein. The Court of Appeals properly held that the "amended answer" of the Debtor was a nullity, but held further that, even had it been timely, "it would not alter the result since the debtor reiterated its consent to reorganization and its inability to meet its debts as they matured" (petition, p. 39). Clearly, the Debtor was not entitled to withdraw that consent and to file the proposed answer *de novo* months later.

5. The petitioner's assertions of conflict of the decision below with the decisions of this and other courts are frivolous. The cases cited are not decisions on the same matter, and are wholly consistent with the decision of the Court of Appeals herein.

Conclusion

For the reasons stated, the petition for a writ of certiorari should be denied.

Respectfully submitted,

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McGOLDRICK, DANNETT,
HOROWITZ & GOLUB,
Of Counsel.

Dated: May 29, 1956.

Appendix A

PERTINENT PROVISIONS OF THE BANKRUPTCY ACT

Sec. 3. Acts of Bankruptcy. Acts of bankruptcy by a person shall consist of his having * * * (6) admitted in writing his inability to pay his debts and his willingness to be adjudged a bankrupt.

Sec. 126. Filing petition; persons entitled. A corporation, or three or more creditors who have claims against a corporation or its property amounting in the aggregate to $5,000 or over, liquidated as to amount and not contingent as to liability, or an indenture trustee where the securities outstanding under the indenture are liquidated as to amount and not contingent as to liability, may, if no other petition by or against such corporation is pending under this chapter, file a petition under this chapter.